

THE BOND BUYER

THE DAILY NEWSPAPER OF PUBLIC FINANCE

Calif.'s Lockyer Says Raters Using Crisis as Excuse to Block Reform

Bond Buyer | Wednesday, October 22, 2008

By [Lynn Hume](#)

The credit rating agencies are using the financial crisis they helped create as an excuse for not putting an end to their discriminatory system for rating municipal bonds, California Treasurer Bill Lockyer told the chairman of a House panel that is scheduled today to examine the roles rating agencies played in the financial crisis.

"For far too long, the method for rating municipal bonds has produced profits for the agencies, bond insurers, and investors, but bilked taxpayers," Lockyer said in a statement accompanying a letter he sent yesterday to Rep. Henry Waxman, D-Calif., chairman of the House Oversight and Government Reform Committee. "With state and local governments across the country struggling to cope with the contagion from our economic ills, now is the time for taxpayers to gain equal status with corporations. Unfortunately, the agencies are using the crisis they helped create as an excuse to delay reform. Taxpayers should have to wait no longer for simple fairness. Congress should not hesitate to act."

In his two-and-a-half-page letter, Lockyer described for Waxman his eight-month crusade to get the credit rating agencies to overhaul their rating systems for muni bonds.

Lockyer claims that rating agencies have held municipal issuers to higher rating standards than corporations, despite the fact that muni bonds have lower default rates. He is particularly upset that many issuers have had to obtain insurance or other credit enhancement at great cost for their bonds to make them eligible as money market fund investments. The Securities and Exchange Commission's Rule 2a-7 requires that money market funds hold only securities with ratings in the double-A category or higher.

"The irrationality of the dual system the agencies employ in rating municipal and corporate bonds might best be illustrated by some recent actions of Standard & Poor's," Lockyer told Waxman in the letter. "At the beginning of June, that agency rated both the state of California's general obligation bonds and Lehman Brothers' debt the same: A-plus. Yet how could any rational person believe that a long-term investment in Lehman Brothers was as safe as a long-term investment in California?"

Lehman Brothers was forced last month to file for bankruptcy. Yet Standard & Poor's ratings seem to suggest "that the full faith and credit of the largest state in the country was just as risky as a highly leveraged investment bank with a huge portfolio of subprime mortgages," he told Waxman.

The House Financial Services Committee also has pressured the agencies to change their rating systems for muni bonds. In July, the committee passed the Municipal Bond Fairness Act, which directs the SEC to require registered credit agencies to rate municipal bonds on the same scale as corporate and other debt, based on the likelihood of repayment.

Moody's Investors Service and Fitch Ratings had pledged to recalibrate their municipal ratings beginning this month but announced they were postponing their plans because of the financial turmoil.

"I believe this is a huge mistake and am very disappointed," Lockyer told Waxman. "The economic crisis points out more than ever the importance of ratings reform. As investors lose trillions of dollars in the stock market, and have justifiable fears about investing in corporate bonds, the rating agencies have an even greater responsibility to assign accurate ratings that inform investors of the relative safety of municipal bonds. [Standard & Poor's], in contrast, remains in a state of denial."

A spokesman at Standard & Poor's said that the agency "is committed to providing investors and the market with independent and quality ratings opinions" and "use[s] the same rating scale across all of the sectors we rate, including U.S. public finance."

This global scale "is designed to serve as a common language for evaluating and comparing creditworthiness across all major sectors and geographies," the spokesman said, adding: "Since 2001, we have made more than 6,300 upgrades on entities in the public finance sector due to a combination of criteria changes and strong credit performance."

© 2008 The Bond Buyer and SourceMedia Inc., All rights reserved. Use, duplication, or sale of this service, or data contained herein, except as described in the subscription agreement, is strictly prohibited. Trademarks page.

Client Services 1-800-221-1809, 8:30am - 5:30pm, ET

For information regarding Reprint Services please visit: http://license.icopyright.net/3.7745?icx_id=20081021H5AFPRH8